

September xx, 2009

Mr. Kelly C. Bowers
 Senior Assistant Regional Director
 Securities and Exchange Commission
 Los Angeles Regional Office – 11th Floor
 5670 Wilshire Boulevard
 Los Angeles, California 90036-3648

Dear Mr. Bowers:

This is in response to the recommendations contained in the Second Annual Report of the Independent Consultant to the City of San Diego dated April 24, 2009 (Report). The City and the San Diego City Employee Retirement Systems (SDCERS) have already taken corrective actions or begun the process to implement many of these recommendations.

Financial Control Structure

Audit Committee

Recommendation 1:

The new Audit Committee should take the actions necessary to complete its formation and the City should adopt the ordinances necessary to confirm that the new Audit Committee has the full scope of authority of its predecessor Council Audit Committee.

Response 1:

The City concurs with this recommendation. The reconfigured Audit Committee (comprised of two Council members and three independent public members with financial and accounting expertise) has been meeting regularly since January 12, 2009. The City Attorney's office has prepared an ordinance to further specify the duties and powers of the Audit Committee, as granted by the citizens of the City of San Diego with the adoption of Proposition C in the June 3, 2008 election. While these duties and responsibilities are similar to those of the former Council Audit Committee, the proposed ordinance further clarifies the responsibilities of the new Audit Committee in conformance with y are limited by the authority contained in San Diego City Charter section 39.1. The proposed ordinance was approved by the is anticipated to be considered by the Audit Committee on August 31, 2009, and forwarded to the City Council for consideration in September the fall of 2009. ~~If approved, the ordinance will be forwarded to the City Council for consideration.~~

Page 2
Mr. Kelly C. Bowers
September xx, 2009

Internal Audit Function

Recommendation 2:

The City should continue the effort to significantly increase the staffing of the internal audit function in order to permit effective internal auditing to be accomplished, including an assessment by the City Auditor of staffing needs, and the City Auditor should periodically report on progress to the Audit Committee.

Response 2:

Early in 2008, the Audit Committee directed their professional audit consultant (Jefferson Wells) to examine the number of City auditable units, the citywide risk assessment developed by the Internal Auditor, and audit staffing levels at other comparable cities in order to recommend appropriate staffing levels for the City's new Audit Department. In their report dated March 6, 2008, Jefferson Wells recommended that Audit Department staff be increased to 24.5 full-time employees and that the Auditor comment on how the increase could be accomplished. The City subsequently developed a plan to reach the recommended staffing levels over a three to five year period.

Despite the difficult budget situation facing the City, the Mayor, the City Council, and Audit Committee have shown a strong commitment to build the capacity of the City Auditor's Office. Between FY 2008 and FY 2010, the City more than tripled the number of auditors and FTE's assigned to the Auditor's Office. In fiscal year 2008, five full time positions (FTE), including three auditors, were assigned to the Auditor's Office. In fiscal year 2009, the City increased Auditor staffing to 11 FTE's, including eight auditors. In Fiscal Year 2010, the City added six principal auditor positions and one fraud investigator position to the City Auditor's budget. As a result, the City Auditor now has 14 Principal Auditors and total department staff of 18.0 FTEs.

The City Auditor has kept the Audit Committee and City Council aware of the need to provide additional audit resources to his office. Specifically, in April 2009, the City Auditor communicated the department's staffing needs to the Audit Committee and in May 2009, he communicated his staffing needs to the City Council.

Whistleblower and Hotline Complaint System

Recommendation 3:

The Audit Committee should evaluate the operation of the hotline to ensure that it is operating effectively as intended with respect to complaints and concerns regarding financial control or financial and auditing matters, and that matters reported to the hotline, especially those that are fraud related, are being appropriately referred and handled.

Page 3
Mr. Kelly C. Bowers
September xx, 2009

Response 3:

Responsibility for the administration of the hotline complaint system transferred from the Mayor's Office of Ethics and Integrity to the City Auditor in July of 2008. Since the transfer of hotline administration, the Audit Committee has maintained an active role in evaluating and monitoring the operation of the fraud hotline. On a quarterly basis, the City Auditor issues an update report to the Audit Committee and public on the number of complaints received, investigated, and complaint status and disposition. In turn, the Audit Committee places on its meeting agendas periodic updates from the City Auditor regarding the fraud hotline and handling of fraud-related complaints. ~~Further,~~

The Audit Committee has also involved the City Attorney's Office in its evaluation of the hotline to ensure that the hotline complies with all applicable laws and regulations. On October 20, 2008 the Audit Committee reviewed and approved the City Auditor's updated fraud hotline administrative plan and procedures. Additionally, the Audit Committee recommended and the City Council approved the City Auditor's budget request to add a Fraud Investigator dedicated to the hotline beginning in FY 2010.

Formatted: Indent: Left: 0", Adjust space between Latin and Asian text, Adjust space between Asian text and numbers, Tab stops: Not at 0.25"

Improper Influence Ordinance

Recommendation 4:

The City should proceed expeditiously, but no later than 60 days from the date of this Report, to adopt an improper influence ordinance.

Response 4:

The Improper Influence Ordinance was initially heard on June 22, 2009 and revisions were requested. The Ordinance was re-introduced by the City Council on July 27, 2009. The City Council adopted the Ordinance following a second reading at Council on September 1, 2009. The Ordinance second reading will occur in September and will become affective 30 days ~~thereafter~~ the Mayor subsequently signs the Ordinance (within 10 days of the second reading) which should be in early October 2009.

ICOFR Initiative

Recommendation 5:

Given the current status and the priority being devoted to the OneSD project, it is important that the City establish a realistic schedule for completing the ICOFR effort and for testing and assessing the ICOFR remediation, as contemplated by the Kroll Report. The testing and assessment process should be divided into three phases first, in anticipation of the fiscal 2010 audit; the outside auditor should evaluate the ICOFR design (this will both motivate and assist completion of the work); second, as part of the fiscal 2010 audit, the outside

Page 4

Mr. Kelly C. Bowers

September xx, 2009

auditor should assess through an integrated audit and report on the effectiveness of the operation of the ICOFR process; and third, in connection with the fiscal 2011 audit, the City should have an external assessment of the effectiveness of its ICOFR (comparable to an independent auditor attestation required for SEC reporting companies under Section 404(b) of the Sarbanes-Oxley Act). This external assessment could be made by the City's regular outside auditor or by another qualified party. To the extent there are deficiencies or weaknesses identified in any of these testing activities, a third party consultant could be retained to assist with the remediation. Although later than contemplated, this procedure is consistent with the Kroll recommendation on independent auditor assessment of the City's internal controls.

Response 5:

The City concurs with this recommendation. Management is meeting with McGladry on an on-going basis in regards to the design and full implementation plan for the documentation, training and monitoring of Internal Controls Over Financial Reporting (ICOFR).

With the current budget constraints facing the City of San Diego, necessary staffing resources are being impacted across all departments and may have an impact over the ICOFR project as well, in terms of extending the completion timeline. While significant progress will be made in FY2010 on the ICOFR project, management will assess in April 2010 whether or not there is a sufficient enough ICOFR framework in place to warrant expending funds to have an external effectiveness audit of its ICOFR process. While we agree that an independent external audit of internal controls could be a useful assessment, we also

understand that there needs to be a critical mass of ICOFR documentation in place in order for an external audit to be meaningful. We will continue to assess our readiness in regards to this recommendation point.

Management concurs that an external assessment audit of the effectiveness of the ICOFR process as part of the FY2011 audit would be appropriate. However, since there is no requirement for the City to be compliant under the terms of the Sarbanes-Oxley Act, management would propose that the assessment audit over internal controls be customized to our municipal government operations. We view this as a more effective solution towards understanding the effectiveness of our ICOFR process.

- *On a near basis:*

Recommendation 6:

Executive oversight should be applied to monitor the achievement of ICOFR documentation objectives against the established timeline. The prioritization of this effort over the next 60 days should be communicated and maintained through executive mandate.

Response 6:

A timeline is currently being drafted and will be available for review by August 31, 2009. The timeline will document milestones for documenting ICOFR as well as reporting on testing of selected ICOFR objectives that have already commenced.

Page 5

Mr. Kelly C. Bowers

September xx, 2009

Recommendation 7:

Plans should be developed to obtain additional resources should the ICOFR timelines be challenged by resource constraints with City personnel charged with responsibilities in connection with the OneSD initiative and whose efforts are necessary on the ICOFR effort.

Response 7:

The City concurs with this recommendation. Exploration into several options is currently underway. (information being added) The City will bring in external resources if necessary to assist City personnel with achieving the ICOFR objectives within the timeframe outlined.

Recommendation 8:

The City Council should approve the lease financing amounts required for the OneSD project so that it can be successfully implemented.

Response 8:

The City Council approved the lease financing amounts at the May 12, 2009, Council meeting as Ordinance 19860.

Financial Reporting Enhancements

Review of CAFRS

- *The Audit Committee should review within 60 days of the date of this Report and improve as necessary the procedures for review of the City's CAFR, including:*

Recommendation 9:

The City should establish a schedule for completion of the CAFR process before the continuing disclosure deadline and sooner if possible.

Response 9:

The City concurs with this recommendation. On March 26, 2009 the City became current with six years of overdue CAFRs by issuing the fiscal year ended June 30, 2008 report. The City is now on a routine CAFR year end schedule which will ensure the CAFR audit is issued before December 31, 2009. This is well before the continuing disclosure deadlines, which start at the end of March, and also allows the City to submit for the Government Finance Officers Association "Certificate of Achievement for Excellence in Financial Reporting" program. A brief summary of major milestone dates is as follows:

- July 24, 2009: fund closing deadline
- August 28, 2009: fund level financial statement preparation deadline

Page 6

Mr. Kelly C. Bowers

September xx, 2009

- September 30, 2009: first draft of CAFR to external auditor, Macias, Gini & O'Connell (Macias) (includes all notes and Management Discussion and Analysis)
- November 6, 2009: first round of comments from Macias
- November 13, 2009: first full CAFR to the City's Disclosure Practice Working Group (DPWG)
- December 4, 2009: Partner Standards Review (PSR) comments from Macias and final DPWG review
- December 11, 2009: DPWG certificate
- December 18, 2009: Opinion letter
- Early January 2010: Review by Audit Committee
- Late January 2010: Docket at City Council to receive and file
- Upon City Council action, posting of CAFR on City's investor webpage

Recommendation 10:

The CAFR process should reflect the requirement for legending the CAFR and Refraining from posting it on the City's investor information webpage upon its release but before completion of the review process.

Response: 10

The CAFR schedule that has been established for the fiscal year 2009 audit and as operational procedure for future years will allow sufficient review time for the DPWG, the Audit Committee and the City Council before the CAFR is posted on the City's investor webpage. As presented in the preceding response, the City's CAFR schedule will include sufficient time for DPWG certification, the Audit Committee review, and the City Council's

Page 7
Mr. Kelly C. Bowers
September xx, 2009

review and action to receive and file the City's CAFR. The City's practice is to post the CAFR on the City's Investor Page only after the Council has received and filed the CAFR. This is in accordance with the guidance provided by DPWG for making the postings on the Investor Page. In conjunction with the release of the audit opinion and the public release of

the CAFR for Audit Committee review, CAFRs will initially be posted on the City Comptroller's page on the City's website only with cautionary statements. ¹The link to CAFR is established on the Investor Page by the Debt Management Department only after the City Council receives and files the CAFR. Information that is intended to reach the investing public, bondholders, or any other members of the investment community is only posted on the City's on the Investor Page.

Recommendation 11:

The Audit Committee and DPWG should consider a process that allows designated members of the Audit Committee, on an ad hoc basis, to have input on the CAFR before it is publicly released.

Response 11:

The City concurs with this recommendation. The draft Audit Committee Ordinance discussed in the Response to Recommendation #1 contains language that would permit the Audit Committee to designate a representative to attend meetings of DPWG at which the City's CAFR will be considered. This would allow the designated representative to review the CAFR prior to its public release and have access to the deliberations of the DPWG regarding any changes incorporated into the final CAFR, while at the same time protecting the CAFR review process and complying with the Brown Act.

Improved Discussion and Analysis

Recommendation 12:

The City, on an ongoing basis, should continue to improve the quality of its financial disclosure by providing analysis that facilitates an understanding of the City's financial statements and its financial condition, financial results, liquidity and capital needs, including the risks faced by the City.

Response: 12

The City concurs with this recommendation and has made considerable progress in this area. The City has been improving its "Letter of Transmittal" and "Management's Discussion and Analysis" with each issued CAFR (fiscal years 2006-2008). Specifically, in the 2007 and 2008 CAFRs, we have increased the detailed discussion of the City's financial condition in

¹ The cover page of the CAFR contains the following statement: "This document has not been submitted to the Audit Committee for consideration nor has it been received and filed by the City Council. "

Page 8

Mr. Kelly C. Bowers

September xx, 2009

the coming fiscal years, including detailed discussion regarding the projected General Fund deficit (current year) and actions taken to remediate that projected deficit. Additional analysis and disclosure also include the City's liquidity position and changes from the previous year, the City's reserve policies and funding goals compared to actual reserve funding progress, monthly SDCERS investment portfolio updates and projected impact on the City's pension payment and funded position, five-year financial outlook detailed discussion and analysis of the eight significant areas of funding, among many other improvements. We are committed to closely reviewing our disclosures and financial data every year. By reviewing best practices in private sector and municipal financial statements, we seek continual disclosure practice improvements to increase transparency in analysis and reporting. As we implement new accounting standards each year, we will maintain accurate, reliable and timely financial reporting. The City is now a leader among municipal governments in its disclosure practices and reviews.

Recommendation 13:

In connection with forward-looking statements, such as forecasts, projections and statements of future intent, the City should evaluate the adequacy of its inclusion of appropriate cautionary statements that would put those forward-looking statements in proper context.

Response: 13

The City concurs with this recommendation. The City has made steady progress both in terms of improving the analysis available in the CAFR, particularly in the Letter of Transmittal, with respect to City management's assessment of the City's overall financial condition and in offering appropriate cautionary language regarding the use of forward-looking information in City documents. However, such cautionary language, which has been incorporated into the investor information webpage and in City documents such as rating agency presentations, has not been explicitly incorporated into the CAFR. The City will work with DPWG and the City's outside disclosure counsel to craft suitable cautionary language to be used in the CAFR.

Loss Contingencies and Risk Assessments

Recommendation 14:

The City, through the City Attorney's Office and the Risk Management Department, should continue to improve its systems for dealing with loss contingencies for financial reporting purposes in order to remedy any deficiencies noted by the City's independent auditors to the extent not already remedied.

Response: 14

The City concurs with this recommendation. Deficiencies with respect to the City's process for identifying and assessing loss contingencies, particularly regarding litigation, were noted in the Kroll Report. In response to the Kroll Report and in order to mitigate those deficiencies, the City implemented a procedure requiring quarterly meetings between the

Page 9

Mr. Kelly C. Bowers

September xx, 2009

Risk Management Department and the City Attorney's Office to ensure that both responsible offices are fully apprised of all outstanding claims against the City and are aware of the progress of those claims to date. In order to ensure that contingencies are appropriately accrued, a representative of the Chief Financial Officer attends those meetings. The City Attorney's Office has also developed a comprehensive process for the preparation of City's FAS 5 letter which has greatly enhanced the quality of the information provided to the City's independent auditors which is disclosed in the City's audited financial statements. While the City continues to refine its process for evaluating loss contingencies, the City is not aware of any particular issue raised by the independent auditors.

Disclosure Practices Working Group (DPWG)

Shelf-like Disclosure

Recommendation 15:

The DPWG should continue to evaluate its processes and procedures to ensure that it has the correct composition to fulfill its role and to streamline its operations so that it operates efficiently and effectively without sacrificing the thoroughness of its review of the City's disclosures.

Response 15:

The City concurs with this recommendation. DPWG is evaluating the effectiveness and efficiency of the City's disclosure practices and procedures which were fully implemented for the first time with the public issuance of water revenue bonds in January 2009 and in three subsequent public issues. DPWG is also evaluating the composition of the group to more accurately reflect roles and responsibilities within the City, particularly in light of the adoption of Proposition C, which, among other things, separated the duties and

responsibilities previously combined in the Office of the Auditor and Comptroller by creating a new City Auditor position and consolidating all financial management responsibility under the Chief Financial Officer. The City Attorney's office, in cooperation with DPWG, intends to bring appropriate amendments to the Disclosure Ordinance to the City Council in the fall of 2009.

Recommendation 16:

Related to this, the DPWG, working with the Audit Committee and the City Attorney's Office, should rationalize the process for review of related entity and component unit disclosures and financial reports so that the right resources are brought to bear in an efficient and effective way.

Response: 16

The City concurs with this recommendation. The City Attorney and the City's outside Disclosure Counsel provided the City Council with a memorandum dated July 9, 2008, which sought to provide guidance to the Council regarding their responsibility for the review of various disclosure documents, including those of City related entities. This memorandum,

Page 10

Mr. Kelly C. Bowers

September xx, 2009

as amended, concluded in relevant part, that DPWG should review documents of the City's related entities to the extent they constitute "disclosure documents" as that term is defined in Municipal Code section 22.4107(a)(1). Subsequent discussions at the Audit Committee and the City Council led DPWG to adopt certain ad hoc procedures for the review of the audited financial statements of the Redevelopment Agency. In the spring of 2009, DPWG assembled a group including several members of DPWG and individuals responsible for financial management functions at the City's Redevelopment Division, the Centre City Development Corporation and the Southeastern Economic Development Corporation to review the audited financial statements of the Redevelopment Agency. DPWG intends to codify the Redevelopment Agency review procedure in the Disclosure Controls and Procedures and will establish similar procedures for the Housing Commission.

Recommendation 17:

The DPWG should consider ways to enhance the confidence of Audit Committee members and Council Members in the DPWG process in compliance with the Brown Act and without diminishing the effectiveness of the DPWG.

Response 17:

The City concurs with this recommendation. DPWG is evaluating ways to incorporate both the Audit Committee and the City Council into the disclosure review process in order to provide the members of those bodies greater confidence in the City's disclosure review process. As discussed above, the proposed Audit Committee ordinance will provide for a representative of the Audit Committee to participate in meetings of the DPWG at which audited financial statements are considered. DPWG is also considering how ways to accommodate City Council concerns regarding the City's disclosure review process.

Recommendation 18:

An SDCERS official should participate as necessary in a session of the DPWG at which pension-related disclosures are addressed.

Response 18:

The City concurs with this recommendation. Municipal Code Section 22.4110 requires officer and employees of SDCERS to assist DPWG as requested, including appearing before DPWG. Currently, DPWG solicits input from SDCERS with respect to disclosures relating to the retirement system to the extent such information is included in City disclosure documents and requests certifications from SDCERS management regarding those disclosure. DPWG will request the presence of a representative of SDCERS, in person or via telephone, during meetings which include substantive discussions of disclosures related to SDCERS.

SDCERS officials have contributed to the review of pension related disclosures in various ways in the preparation of the City's CAFRs for 2003-2008: SDCERS officials have reviewed and commented on disclosure materials, participated in DPWG conference calls and met with City staff to review pension related information for disclosures. The City expects this participation to continue.

Page 11
Mr. Kelly C. Bowers
September xx, 2009

Recommendation 19:

The City, with the assistance of the DPWG, should continue to evaluate steps toward a shelf like disclosure system, including expanded use of the City's website, to improve the quality and timeliness of its reporting to the financial markets on an ongoing basis and to permit the efficient access to the capital markets for needed financing.

Response: 19:

The City continues to evaluate the potential for establishing a shelf-like registration regime for City debt issues. The Independent Consultant discussed such a regime with DPWG on April 28, 2008. The two principal objectives or benefits of shelf-like registration discussed were improved quality of City disclosures due to timely periodic reporting and greater speed to market, allowing for timing market access to achieve cost savings. Two particular documents were discussed in terms of offering potentially useful periodic reporting: the City's financial statements and the City's "Appendix A", a document that is typically appended to City official statements and which contains a variety of demographic and economic data on the City and the surrounding area.

The City remains concerned that the amount of staff time required to maintain such a regime may outweigh the potential benefits. However, the City recognizes that certain efficiencies with respect to financial reporting will naturally flow from the activation of the City's ERP system which occurred on July 1, 2009. The City needs additional time to fully understand the system's capacity to aggregate financial data and present such data in a reliable and useful format. The City also notes that, with respect to Appendix A, the City substantially relies on County and State sources for data and that such data may not be reported to the City on a timely basis. For instance, taxable sales data typically lags by three quarters. As noted by the Independent Consultant, the City has been providing monthly data on the asset value of the pension system and recognizes the value of developing a risk based appendix that addresses those issues faced by the City that are of the greatest interest to investors. The City intends to prepare a proposal for periodic disclosure by the second half of fiscal year 2010.

Recommendation 20:

The DPWG should assess the effectiveness of its review of the form and content of "press releases, ... web-site postings, and other communications reasonably likely to reach investors or the securities markets" as set forth in Section 22.4107(a)(1) of the Municipal Code, recommend changes, if any, to reflect actual practices within the City and develop proposed guidelines for City officials regarding press releases.

Response 20:

The City concurs with this recommendation. The 2008 Annual Report of DPWG addressed certain issues regarding the Municipal Code requirement that DPWG review press releases and other documents reasonably likely to reach the investing public. That report recommended that the requirement be removed from the Code and that all City officials be

Page 12

Mr. Kelly C. Bowers

September xx, 2009

provided with guidelines for drafting and disseminating press releases addressing City financial information. DPWG intends to develop such guidelines with the assistance of the City's outside disclosure counsel. Required Municipal Code amendments will be included in the amendments to the Disclosure Ordinance referred to above.

Role of Counsel in Legal Compliance

Recommendation 21:

The City should evaluate the role of legal counsel that will foster the ability of City officials to consult with and obtain legal advice based upon a relationship of trust and confidence designed to promote legal compliance.

Response 21:

The City has made significant progress with respect to the relationship between City management, City Council and the City Attorney's Office as counsel to the City. The current City Attorney recognizes that, pursuant to the City Charter, he is counsel to the City as a municipal corporation and chief legal advisor to all City departments and offices. While the relationship among independently elected officials in a municipal context is not identical to the relationship between management and corporation counsel in a private organization, the clarification of the attorney-client relationship between City management and the City Attorney's Office has ameliorated many of the tensions noted by the Independent Consultant in his previous report. The City also notes that John McNally of Hawkins, Delafield & Wood has served as general disclosure counsel to the City since 2004 and has been instrumental in establishing City policies to promote compliance with federal securities laws.

San Diego City Employees' Retirement System (SDCERS)

Recommendation 22:

SDCERS, in conjunction with the City management and DPWG, should evaluate the communication process and information flow between SDCERS and the City and adopt necessary modifications, if any, to this process to ensure the complete and timely flow of pension and benefit-related information to the City necessary for fiscal planning and the preparation of the City's financial statements.

Response 22:

The City concurs with this recommendation and considerable improvement has occurred in the flow of information. SDCERS has participated in the preparation of the City's CAFRS by providing extensive review and comment on the required pension information and

disclosures. The SDCERS CFO participates in the DPWG review meetings either in person, by phone or by submitting comments to draft CAFR information for DPWG review.

In September 2008 SDCERS began submitting to the City unaudited month end market valuations for the pension assets and provided review and analysis of those valuations by the

Page 13

Mr. Kelly C. Bowers

September xx, 2009

pension system's actuary. The City uses this information to post monthly updates on the City's investor webpage approximately 14 days after the end of the month. These updates show the potential impact that changes in the SDCERS plan assets may have on the City's pension contribution, the budget, and the funded ratio of the pension plan based on a hypothetical evaluation of the unaudited market value of the pension assets at month end. San Diego has been receiving pension information each month from SDCERS and has posted this analysis on the City's investor webpage monthly starting in October 2008.

As a result, the City has taken a lead position among cities to produce timely pension disclosure information to investors and the public. Additionally, in the preparation of the City's Five Year Financial Outlook released November 2008, SDCERS and its actuary provided two scenarios that projected possible pension payments over the next five years. Based on broad actuarial assumptions, these scenarios incorporated the recent market downturn and conservative projections of market losses as a basis for future pension payments for 2011 and beyond. These projections of future pension payments have improved the Five Year Outlook of the City and have been an important part of the City's fiscal planning and disclosures. The City will work with SDCERS on pension payment forecasts to include in the next version of the 2011-2015 Five Year Outlook which will be issued in September 2009.

Recommendation 23:

The SDCERS Board should consider steps for the selection of SDCERS' actuary that ensure the independence and objectivity of the actuary as part of best practices for actuary retention.

Response 23: **SDCERS**

Recommendation 24:

The City, working with SDCERS and with the assistance of an experienced pension consultant, should continue to explore the range of alternatives for funding the City's pension and post-retirement benefits commitments, but it should do so based only on sound actuarial principles, consistent with prevailing practices in similar entities, with total transparency and without impairing the integrity of the pension system.

Response 24:

The City concurs with this recommendation. The Mayor and the SDCERS Board are City is independently studying the alternatives for funding the pension system using sound actuarial techniques ~~and~~ by reviewing the actions other large pension systems are taking to change actuarial techniques in light of the decline in market assets. This is an SDCERS Board decision that will need to be made no later than October 2009. The ~~Mayor~~City will provide comments to the SDCERS Board in a manner completely transparent to the public.

Recommendation 25:

Page 14

Mr. Kelly C. Bowers

September xx, 2009

SDCERS should continue to develop and implement a comprehensive training program for its trustees and staff, including training in pension finance and investing and in prudent trustee requirements. It should report periodically on these training activities.

Response 25: **SDCERS**

Hiring of Necessary Personnel

Recommendation 26:

The City should promptly fill the vacancy in the position of Comptroller.

Response 26:

The City Comptroller position was filled on June 18, 2009. The new City Comptroller is a licensed CPA with experience in implementing internal controls for private sector companies.

Fiscal Integrity

Recommendation 27:

The City should assess the value of its current Five- Year Financial Outlook as a planning tool, and consider use of additional planning tools, for ensuring that the City is able to meet its goals for providing services to the citizens of San Diego at a cost they are willing to bear.

Response 27:

The City concurs with this recommendation. The City's Five-Year Financial Outlook (Outlook) is a multi-year view of the City's General Fund which outlines the financial challenges facing the City as well as developing and implementing solutions in meeting these challenges. ~~It is a multi-year planning tool which enables the City to set meaningful objectives with realistic timeframes for completion.~~ The Outlook is a planning tool that ~~incorporates the City's fiscal policies and~~ covers a wide range of issues including revenue and expenditure analysis, user fee cost recovery goals, investments, debt management, ~~contracting for services,~~ and levels of working capital (fund balance). The City continues to assess ways to improve the value and accuracy of the Outlook. The Office of the Independent Budget Analyst has performed independent reviews and analyses of each of the three prior Outlooks and has made suggestions for enhancement such as: a discussion of "risks" to the Outlook; more detailed information on underlying assumptions; impacts of various expenditure assumptions; the inclusion of costs associated with new facilities coming on line during the forecast period; the magnitude of a fiscal obligation liability such as deferred maintenance; alternative actions to consider for addressing the projected deficits; and a comprehensive discussion of future unfunded needs. The Outlook reinforces the City's commitment to long-term fiscal health by looking beyond a one-year time horizon in its ability to fund operating programs.

Page 15

Mr. Kelly C. Bowers

September xx, 2009

~~The Outlook is a “living” document where underlying assumptions are being constantly reviewed and adjusted when necessary. If changes are necessary and/or actual results differ from projections in the Outlook, they are comprehensively assessed, analyzed and explained.~~

The latest Outlook released in November, 2008 included a sensitivity analysis for revenue projections which had not been included in prior years' Outlooks. A sensitivity analysis was applied to all City's major revenues allowing to see the trends of growth rates while

developing “pessimistic”, “normal”, and “optimistic” scenarios affecting projected revenue receipts. Also, for the first time, in the November 2008 Outlook, a sensitivity analysis was applied to the City's pension payment which assumed a significant loss in the market value of pension system assets and how this negative impact of investment losses would affect the General fund over the next five years. In addition, the November 2008 Outlook included a comprehensive risk assessment of the City's revenues and expenditures and discussed risks and opportunities that affect fiscal decisions and the City's ability to accomplish its strategic goals over the next five-year period. A more sophisticated and enhanced sensitivity model will be used in future Outlooks for the development of revenue and expenditure projections.

The City's Five-Year Financial Outlook continues to be a critical planning tool serving as a basis for the preparation of the City's annual budget and will continue to be updated on a regular basis as it has been in the past years.

The City will continue to work with the Independent Consultant to not only implement these recommendations but also to go beyond in order to ensure that the City continues to establish best practices in its financial reporting and ultimate disclosure.

Sincerely,

JERRY SANDERS
Mayor

BEN HUESO
Council President

ML/

Attachments:

cc: Honorable Members of City Council/Audit Committee Members
Jan Goldsmith, City Attorney
Jay M. Goldstone, Chief Operating Officer
Mary Lewis, Chief Financial Officer
Stanley Keller, Independent Consultant
Andrea Tevlin, Independent Budget Analyst